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Author: Glenn P. Jenkins
Harvard University

Title: OPTIONS FOR DEALING WITH DECLINING INDUSTRIES

Summary: The Canadian government has tried almost every conceivable policy to assist declining firms, industries and regions. Such programs have included loans, grants, investment tax credits, special unemployment compensation, early retirement plans, employment tax credits and nationalization. The results have not been impressive. There is always a continuous movement of entrepreneurs, labour and capital to new opportunities and often when an industry is far removed from a major centre this decline has particular regional and employment implications. Policy options are required as much for addressing the social and political problems of declining communities and regions as for declining industries. There have been a number of studies that show that income losses imposed on individual workers, although in some cases not insignificant, appear almost trivial when compared with the government subsidies or higher costs imposed on Canadian consumers. Labour adjustment assistance, particularly in the form of lump-sum payments, has the ability to produce more rapid and economical adjustment for declining industries.

Canada

INTRODUCTION

The continuous movement of entrepreneurs, labour, and capital to new opportunities, higher-wage jobs, and more profitable ventures, and away from lower-wage and less profitable activities, is a fundamental requirement for economic growth and increased employment. This is a natural process that occurs continuously as a response to market forces in the Canadian economy. Usually this operates without any explicit government intervention, or financial assistance from taxpayers.

For a variety of reasons, in certain sectors and firms this adjustment process comes into the focus and purview of governments. Often their response to the prospect of a decline in an activity of a major firm or industrial sector is to attempt to find ways to slow down or halt this adjustment process. One consequence of such actions is that many state-owned enterprises now in existence were formerly private enterprises that were threatened with a major decline, or worse.

When the perceived reason for the decline is the successful competition by foreign producers for sales in the domestic market, the Canadian government often has been willing to impose quotas (voluntary or otherwise), adjust the basis for tariffs, or engage in some other market intervention that forces consumers and other producers to buy the item from a domestic producer at a higher price. In other cases, usually under the banner of adjustment assistance and modernization, governments will attempt to subsidize the investment costs of certain firms so that they can face the competition from other suppliers, both domestic and foreign.

In Canada, there is no shortage of examples of all three types of intervention. Canadair and de Havilland were made Crown corporations in order to avoid the collapse that would have happened if the large government subsidies had been withdrawn. Bilaterial quotas on garments and textiles, global quotas on footwear, and voluntary quotas restricting the importation of Japanese automobiles are all examples of attempts to make domestic consumers and other producers who use these items pay more in order to maintain or increase the level of activity in certain specific sectors. In addition, government grants to textile companies and to pulp and paper firms have often been made in order to maintain regional operations.

COMMUNITY VERSUS INDUSTRIAL ADJUSTMENT

A decline in the demand for an industry's or firm's product naturally results in a decline in the demand for the labour and the capital invested in the sector. Productive inputs that have good opportunities elsewhere (skilled workers, competent managers, funds for new investment) move away from the industry, while other inputs (such as high-seniority workers and the existing plant and equipment) will tend to experience lower real wages and lower rates of return.

If such an adjustment takes place in large urban labour markets, the alternative options for the employment of these factors in their existing skills are higher, and the opportunities for retraining of labour or undertaking new lines of business are more readily available than in the smaller regional communities.

In communities that depend heavily on one or more declining industries, substantial losses are usually imposed on both the owners of real estate and the owners of service sector firms. The magnitude of their loss in wealth and the public outcry accompanying it can be greater than that experienced by the industry directly affected.

With some notable exceptions (e.g., automobiles), most industries that experience a period of adjustment have usually faced adverse market pressures for many years. As a consequence the capital stock in the firms are generally largely depreciated by the time that the problem is acute enought to elicit government action.

The labour forces of these sectors are also very aware of the trends in the market demand for goods produced. As a result, often the age distributions of the employees become highly concentrated in the older groups. There may also be a relatively large group of very young workers who have little intention of remaining in the sector or the region for the rest of their working lives. In contrast, those in the age group from 30 - 45 usually quickly seek alternative employment for fear of being laid off permanently from the declining firm at a time in their life when they have heavy financial responsibilities. In addition, relocation becomes personally more costly, and financially less rewarding, if they are forced to move when they are older. When the labour force has developed this pattern the income losses suffered by the younger workers are usually modest or non-existent. While older workers may suffer greater annual income losses, it is for a shorter duration because they will soon be of retirement age.

In the real estate and service sectors the depreciation of the capital stock and self-selection of workers often does not occur. Even with fluctuating levels of employment in the

economic base activities of the community, the generous unemployment insurance and welfare provisions in Canada tend to maintain the level of demand for the trading and service sectors at a fairly high level.

In the Canadian context, policy options are required as much for addressing the social and political problems of declining communities and regions as for declining industries. If a consensus could be reached on the level that the Canadian taxpayers would be willing to finance the preservation of the existing regional distribution of economic activity and communities, then the appropriate policies for dealing with the declining or expanding industries within the Canadian economy would be greatly facilitated. Given the nature of the political economy of Canada, it is highly unlikely that such a consensus will be reached.

Even if no national consensus could be obtained on this issue, a better understanding needs to be developed of the trade-offs that the economy is experiencing when policies are implemented that attempt to preserve traditional regional activities and communities. Economic costs are incurred to provide extra benefits to those unemployed in the slow-growth regions, to subsidize investments in industries that would otherwise not be competitive, and when all Canadians have to bear the high costs of protecting certain sectors from the competition of international trade. Employing the country's resources in this way, rather than allowing them to find their best use through competition in the marketplace, is likely to lead to a slower rate of economic growth in Canada and to a lower level of employment. While the objective of such policies is to preserve jobs, the economy-wide result is to take resources away from the creation of better jobs with better futures.

LABOUR ADJUSTMENT

The focus of much of the concern related to industrial decline is on the displacement of the labour force in these sectors. If these workers cannot find alternative employment quickly at similar wages, they will suffer an income loss, and a political problem is created.

Recently, a number of studies have been undertaken in Canada to measure the actual financial loss that workers have suffered after being laid off from declining industries. An extensive study, (Glenday, 1982) has been carried out that estimated actual income losses experienced by workers displaced from declining industries across eight different regions of Canada. These workers were laid off during the period between January 1974 and December 1976. The Labour Force Tracking Survey (Department of Industry, Trade and Commerce, 1979), collected information on over 6,000 individuals from over 90 firms. Over 60 per cent of the individuals surveyed were displaced from the textile, clothing and electrical products sectors.

From Table 1 we see that the financial loss of displaced workers was substantially higher for females than for males. However, in no case was the present value of the average income lost in a region greater than $6,800 (1978 dollars). For males, the average financial loss never exceeded $2,500.

Specific estimates are also available for the textile and automobile sectors, as shown in Table 2. The male workers displaced from the textile sector in Shawinigan and Prescott, had an average private income loss of less than $300, irrespective of the age group. Many of the male workers received substantially higher wages in alternative employment following layoff from textile firms. For female workers, the present value of these private income losses ranged from about $2,000 to approximately $6,800.

In the case of automobiles, we find that young workers employed in the automobile sector earn wages that are substantially higher than what they could obtain elsewhere. As a result, the present value of the income loss they suffer is approximately $11,000 for female workers and approximately $13,000 for males. In contrast, older workers displaced from the automobile sector suffer much smaller income losses. Males of about 40 years of age suffer a present value of income loss of only $500 while married women of that age lose about $3,000.

A similar study was carried out to measure the income loss from workers displaced from the aircraft industry (Jenkins and Montmarquette, 1979). These estimates were obtained from a sample of 1,149 individuals displaced from the aircraft industry between 1972 and 1975 (prior to the government purchase of de Havilland and Canadair). The income loss suffered by displaced workers who were less than 45 years of age averaged approximately 7 per cent of the annual wages earned in the aircraft industry. For those between 45 and 55 years of age, the income loss was equivalent to approximately 22 per cent of their previous wage.

While the income losses imposed on individual workers are in some cases not insignificant, they appear almost trivial when compared with the government subsidies or the higher costs imposed on Canadians by policies designed to protect jobs from foreign competition.

Since de Havilland and Canadair were made Crown corporations, the Canadian taxpayers have been saddled with billions of dollars of losses. The hemorrhaging continues.

In 1979, an estimate was made of the cost to consumers of maintaining the bilateral quota system on the imports of garments into Canada (Jenkins, 1981). The cost per man-year of increased employment was estimated to be in excess of $35,000 per annum. The estimated economic waste associated with each person-year of employment was estimated to be in excess of $15,500 per year.

Estimates (Crandall, 1984) have been made of the cost of the voluntary export restraints imposed on Japanese automobiles coming into the United States. This Brookings Institution study estimates that the consumer cost per additional job saved was nearly $160,000 per job per year. The results for Canada are likely to be of a similar order of magnitude.

A comparison of the cost borne by workers when they have been displaced by industries and the cost inflicted on taxpayers through government policies to restrain this adjustment process tends to lead one towards viewing adjustment in a more favorable light.

POLICIES TOWARDS INDUSTRIAL ADJUSTMENT

Government policies which provide assistance to declining firms or sectors when the fundamentals of the marketplace dictate their decline will seldom lead to the development of a competitive economic activity. Because the risk of changes in government policies is very high, few entrepreneurs will make long-term investments to modernize their plant and equipment on the basis of current government policies that create an artificial market environment. Often only the necessary investments are made to keep existing plant and equipment operating. In this way, firms can take advantage of the short-run business opportunities provided by the artificial market situation while avoiding the risk of making long-term financial commitments.

An alternative to policies which attempt to retain existing facilities and sectors would be those that attempt to ease the adjustment costs of moving the factors of production from declining sectors to other opportunities.

In a number of countries, including Canada, programs have been put in place which would financially assist those workers who become displaced from declining firms or sectors. This has sometimes taken the form of supplementary pensions to those taking early retirement or mobility grants to cover the costs of moving to a new labour market. On some occasions, supplementary severence pay provisions are made in order to provide compensation to the displaced workers. The general focus of this type of program has been to ease and facilitate the movement of labour from a declining sector to other more economically viable activities, including retirement.

If such compensation is to be given then it is highly advisable that it be given in the form of a lump sum payment, that has the characteristics of a severance payment. The programs used previously in Canada that provided extended unemployment insurance benefits or made provision for early retirement (Transitional Assistance Benefits Program 1965-76,

Adjustment Assistance Benefits 1971-82) have always had high explicit or implicit tax-back rates if a person found alternative employment. These provisions serve mainly to penalize the industrious people who find alternative employment quickly.

Lump-sum compensation payments to workers also have the advantage of providing them with their own financial means to obtain training, start a small business, or to move to a new location. In this way they can avoid the bureaucratic overhead that is a characteristic of government programs that provide assistance in these areas. To be effective, such a labour adjustment assistance program must have a well-developed implementation mechanism that can determine quickly who is eligible for the benefits and deliver them rapidly.

To date, the Canadian government has tried almost every conceivable policy to assist declining firms, industries, and regions. At various times over the past 15 years it has provided subsidized loans, grants, investment tax credits, special unemployment compensation, early retirement plans, employment tax credits, and nationalization. Its record at picking winners or reviving losers is not impressive.

TABLE 1

PRESENT VALUE OF INCOME LOST BY WORKERS
DISPLACED FROM DECLINING INDUSTRIES BY REGION

(1978 dollars)

Region	Unmarried Male 25 years of Age	Married Male 40 years of Age	Unmarried Female 25 years of Age	Married Female 40 years of Age
Niagara	1,905	1,391	4,870	5,667
Kitchener	2,472	353	6,798	5,348
Toronto	308	1,971	4,947	4,876
Prescott	1,273	235	5,868	4,931
Montreal	800	647	6,258	5,026
Sherbrooke	1,139	460	4,779	4,790
Shawinigan	83	767	5,731	4,489
Quebec City	267	68	3,485	2,951

Source: Glenday, Graham. Labor Adjustment and Trade Liberalization: Costs and Adjustment Policies in the Canadian Context. Ph.D. dissertation. Harvard University, Cambridge, MA, December 1982. Table 2.4., pg. 57.

TABLE 2

PRESENT VALUE OF INCOME LOST BY WORKERS DISPLACED FROM DECLINING INDUSTRIES

(1978 dollars)

Region	Unmarried Male 25 years of Age	Married Male 40 years of Age	Unmarried Female 25 years of Age	Married Female 40 years of Age
Textiles[1]				
Shawinigan	126	261	6,784	4,625
Prescott	10	25	4,553	1,972
Automobiles[2]	12,942	479	10,800	2,921

1. Glenday, Graham and Jenkins, Glenn. "Industrial Dislocation and the Private Cost of Labor Adjustment", Contemporary Policy Issues, No. 4, January, 1984. Table 1, pg. 26.

2. Glenday, Graham and Jahangin, Alan, "Employment Performance and Labor Market Adjustment in the Automobile Industry", Task Force in Labour Market Development, Canadian Employment and Immigration Commission, September, 1981. Table 6.10, pg. 78.

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